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IN THE

Supreme Court of the United States

TRAVELERS CASUALTY AND SURETY COMPANY OF AMERICA,
Petitioner,

v.

PACIFIC GAS AND ELECTRIC COMPANY,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR AMICUS CURIAE AMERICAN INSURANCE ASSOCIATION IN SUPPORT OF PETITIONER

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Amicus curiae American Insurance Association (AIA) respectfully submits this brief in support of petitioner.[1]

When a debtor seeks bankruptcy protection, the various creditors to whom the debtor owes money may file "proofs of claim" in which they seek a determination of the amount of their claim. 11 U.S.C. § 501(a). Any "party in interest," meaning the debtor, another creditor, or any other entity with a stake in the bankruptcy (such as an insurer that may ultimately be asked to satisfy the claim), may file an objection to the "allowance" of that claim. *Id.* § 502(b). If the claim is objected to, the bankruptcy court is required to determine the amount of the allowed claim. Once a claim is allowed, the creditor receives its distribution from the bankruptcy estate, on a *pro rata* basis, according either to the statutory priority scheme, or the terms of a confirmed plan of reorganization, based on the amount of that allowed claim.

[1] No counsel for a party authored this brief in whole or in part, and no person or entity other than the named amicus curiae, its members, and its counsel made any monetary contribution toward the preparation or submission of this brief. Blanket consent for the filing of amicus briefs has been lodged with the Clerk of the Court by both parties.

This case presents a straightforward question: whether a bankruptcy court, in deciding whether (and in what amount) to "allow" a claim, is required, absent contrary direction from the Bankruptcy Code, to make this decision by reference to applicable nonbankruptcy law—typically state law—or whether a background principle of "bankruptcy policy" may authorize the court to adopt a different rule of decision in determining whether to allow a claim in bankruptcy.

AIA, as amicus curiae, submits that, as the statutory language and the decisions of this Court have long provided, questions of claims allowance are to be determined according to the applicable principles of nonbankruptcy law. To hold otherwise, as the Ninth Circuit did below, risks inviting forum shopping. If a valid state law claim could be disallowed in bankruptcy, a debtor might have an incentive to seek bankruptcy protection to gain a litigation advantage over a plaintiff in litigation. By contrast, if bankruptcy law could provide a more generous scheme of claims allowance than otherwise applicable nonbankruptcy law, creditors who are unhappy with the substantive law that would otherwise govern their claims would have an incentive to precipitate a bankruptcy filing, with the intention of winning a friendlier forum for deciding the validity and amount of the debt allegedly owed to them. These incentives may be particularly powerful in cases, such as several pending mass-tort bankruptcies, in which the debtor's business assets are nearly (or entirely) depleted before the bankruptcy filing, but substantial insurance assets remain available to satisfy creditors' claims.

In order to discourage such misuse of the bankruptcy process, this Court should adhere to the well-established principle that, absent a specific provision of the Bankruptcy Code that requires a different result, questions of claims allowance shall be determined according to otherwise applicable principles of nonbankruptcy law.

INTEREST OF AMICUS CURIAE

AIA is the foremost national trade association representing major property and casualty insurers writing busi-

ness across the country and globally. AIA advocates sound and progressive public policies on behalf of its members in legislative and regulatory forums at the state and federal levels and files amicus briefs in cases before federal and state courts on issues of importance to the insurance industry and the insurance marketplace.

Many AIA members issue or have issued insurance policies covering the liability risks of their policyholders. Accordingly, when policyholders seek bankruptcy protection, one consequence of which is that the policyholder's liability (such as its tort liability) may be determined not in the state court system, but rather according to mechanisms established in bankruptcy court, AIA's members are "parties in interest" with a tremendous stake in this bankruptcy process. Indeed, in recent years, some number of bankruptcy cases have been filed in which a principal purpose of the bankruptcy case is to replace a regime of otherwise applicable law that might weed out invalid or fraudulent tort claims, with one that would more liberally provide for the "allowance" of such claims without the scrutiny that might be brought to bear in the tort system. Following the "allowance" of such claims, the claimants would then seek to obligate the insurers to pay this contrived and artificially inflated liability.

As such, AIA and its members have a strong interest in seeing to it that this Court adhere to the established principle that claims allowance shall be determined according to otherwise governing principles of nonbankruptcy law, and thus reduce the incentive for forum shopping claimants to precipitate a bankruptcy filing.

STATUTORY PROVISIONS

11 U.S.C. § 502(b) provides, in pertinent part:

> [T]he court, after notice and a hearing, shall determine the amount of [a creditor's] claim in lawful currency of the United States as of the date of the filing of the petition, and shall allow such claim in such amount, except to the extent that ... such

> claim is unenforceable against the debtor . . . under any agreement or applicable law . . . .

11 U.S.C. § 101(5)(A) provides that the term "claim" means a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured[.]"

STATEMENT OF THE CASE

Prior to Pacific Gas and Electric Company's (PG&E) filing for bankruptcy protection, Travelers Casualty and Surety Company of America (Travelers) had issued surety bonds on PG&E's behalf to various third parties. In connection with the issuance of those surety bonds, PG&E executed a series of indemnity agreements in favor of Travelers (Indemnity Agreements), under which PG&E is obligated to reimburse Travelers for any attorneys' fees that it incurs in connection with Travelers' efforts to enforce or protect its rights incident to the surety bonds. PG&E filed a bankruptcy petition under chapter 11 of title 11 of the United States Code, and Travelers filed an amended proof of claim that asserted its right to recover its attorneys' fees, including fees for work done in connection with the bankruptcy case itself.

The bankruptcy court disallowed Travelers' claim in its entirety on the ground that it was bound by the Ninth Circuit's decision in *Fobian* v. *Western Farm Credit Bank (In re Fobian)*, 951 F.2d 1149 (9th Cir. 1991), which held that claims for attorneys' fees shall be disallowed where the issues litigated are matters of bankruptcy law.

Instead of addressing whether Travelers' claim was unenforceable under "any agreement or applicable law," 11 U.S.C. § 502(b)(1), the lower courts relied on generalized policy justifications to support their rulings. The court of appeals decision below states only that "[t]he resolution of all of these proceedings was governed entirely by federal bankruptcy law" and that "attorney fees are not recoverable in bankruptcy for litigation issues peculiar to federal bankruptcy law." Pet. App. 3a. (internal quotations omitted).

Insofar as a court may reach that result as a function of its construction of the terms of the parties' contract, such an outcome may well be correct as a matter of federal bankruptcy law. But neither the statutory language nor this Court's decisions provide any warrant for the creation, as the Ninth Circuit appears to have done, of a substantive rule of bankruptcy law under which attorneys' fees for litigating bankruptcy issues are subject to *per se* disallowance, independent of state contract law and the terms of the parties' agreement.

ARGUMENT

I. THE ALLOWANCE OF CLAIMS IN BANKRUPTCY IS GOVERNED BY OTHERWISE APPLICABLE NONBANKRUPTCY LAW

A. Section 502 Of The Bankruptcy Code Expressly Directs Bankruptcy Courts To Nonbankruptcy Law

Whether a claim is allowable or not is a matter of federal bankruptcy law under section 502 of title 11 of the United States Code. 11 U.S.C. § 502. This provision, however, directs the bankruptcy court to look to the underlying substantive nonbankruptcy law in order to determine whether the claim is valid, and thus "allowable" in bankruptcy. Specifically, section 502(b)(1) provides that a court shall allow a claim except to the extent that "such claim is unenforceable against the debtor ... under any agreement or applicable law[.]" 11 U.S.C. § 502(b)(1). "Thus, in proof of claim litigation under 11 U.S.C. § 502(b)(1), the validity of the claim is determined under state law." *Johnson* v. *Righetti (In re Johnson)*, 756 F.2d 738, 741 (9th Cir. 1985).

That principle is a familiar one in this Court's bankruptcy jurisprudence. In *Butner* v. *United States*, 440 U.S. 48 (1979), for example, this Court noted that while there are a number of specific ways in which the Bankruptcy Code alters parties' rights under state law, Congress had "generally left the determination of property rights in the assets of a bankrupt's estate to state law." *Id.* at 54.

Butner thus dictates that "in the absence of specific statutory provisions to the contrary, property interests should not be analyzed differently as a result of a party's in-

volvement in a bankruptcy case," and consequently "bankruptcy courts should only modify the usual state-law compendium of rights and remedies if and to the extent that such modifications are specifically authorized or directed by the Bankruptcy Code." *Bank of New England Corp.* v. *Branch (In re Bank of New England Corp.)*, 364 F.3d 355, 363 (1st Cir. 2004).

The federal bankruptcy laws were of course created against the backdrop of nonbankruptcy laws, including state laws regarding property rights. *See In re Chicago, Milwaukee, St. Paul & Pac. R.R. Co.*, 791 F.2d 524, 532 (7th Cir. 1986) ("Bankruptcy law provides a federal machinery for enforcing creditors' rights but the rights themselves are created by state law."); 4 *Collier on Bankruptcy* ¶ 502.03 (15th ed. 2003) ("The validity and legality of claims is generally determined by applicable non-bankruptcy law."). This Court was clear on that point in *Butner*: "Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding." 440 U.S. at 55; *see also Raleigh* v. *Illinois Dep't of Revenue*, 530 U.S. 15, 19 (2000).

This case can and should be decided on that one principle. The resolution of the specific issue presented in this case—whether Travelers may recover attorneys' fees pursuant to the Indemnity Agreements where it has litigated federal bankruptcy issues—turns simply on the question whether such fees would be recoverable as a matter of nonbankruptcy law, here, basic principles of state contract law. As this Court has consistently and repeatedly observed, "'[w]hat claims of creditors are valid and subsisting obligations . . . is to be determined by reference to state law.'" *Raleigh*, 530 U.S. at 24 (quoting *Vanston Bondholders Protective Comm.* v. *Green*, 329 U.S. 156, 161 (1946)); *see also Grogan* v. *Garner*, 498 U.S. 279, 283 (1991) ("The validity of a creditor's claim is determined by rules of state law.").

The bankruptcy scheme takes property rights as it finds them, altering such rights only where Congress has ex-

pressly demanded such change in order to accomplish the policies of the Bankruptcy Code.[2]

B. Federal Law Does Not Require A Different Result

The Ninth Circuit offered no justification for its ruling other than reliance on its decision in *Fobian*, which itself provided scant reasoning for its categorical holding that, as a matter of bankruptcy law, attorneys' fees will not be awarded for litigated issues involving federal bankruptcy law. *Fobian*, 951 F.2d at 1153. The only support provided in the *Fobian* decision is a series of earlier Ninth Circuit opinions refusing to award attorneys' fees in bankruptcy. *See id.* ("'[T]he question of the applicability of the bankruptcy laws to particular contracts is not a question of the enforceability of a contract but rather involves a unique, separate area of federal law.'" (quoting *Collingwood Grain, Inc.* v. *Coast Trading Co. (In re Coast Trading Co.)*, 744 F.2d 686, 693 (9th Cir. 1984))). The effect of the court's holding below is the substitution of federal law for state law with respect to determining the validity of a creditor's property rights, a result this Court has held should not occur "[u]nless some federal interest requires a different result[.]" *Butner*, 440 U.S. at 55. There is no such federal interest here, however, that might justify that result.

While Congress certainly has the authority to preempt contrary state law, U.S. Const. art. VI, cl. 2, there is no suggestion here that state law "interfere[s] with, or [is] contrary to" the Bankruptcy Code. *Hillsborough County, Fla.* v. *Automated Med. Labs., Inc.*, 471 U.S. 707, 712 (1985) (internal quotations omitted).

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[2] A number of specific provisions of the Bankruptcy Code *do* provide that a creditor's allowed claim will differ from that creditor's claim against the debtor under state law. *See, e.g.*, 11 U.S.C. § 502(b)(2) (disallowing a claim for unmatured interest); *id.* § 502(b)(4) (disallowing claim for services of an insider or attorney of the debtor to the extent that the claim exceeds the reasonable value of the services); *id.* § 502(b)(6) (disallowing claims of a landlord for termination of a real property lease, to the extent the claim exceeds a formula set out in the Bankruptcy Code).

State law may be preempted in any of three ways: "State action may be foreclosed by express language in a congressional enactment, by implication from the depth and breadth of a congressional scheme that occupies the legislative field, or by implication because of a conflict with a congressional enactment." *Lorillard Tobacco Co.* v. *Reilly*, 533 U.S. 525, 541 (2001) (citations omitted). No matter what kind of preemption is at stake, however, "[t]he purpose of Congress is the ultimate touchstone of pre-emption analysis." *Cipollone* v. *Liggett Group, Inc.*, 505 U.S. 504, 516 (1992) (internal quotations omitted).

To that end, a congressional intent to preempt state law is not lightly inferred:

> [B]ecause the States are independent sovereigns in our federal system, we have long presumed that Congress does not cavalierly pre-empt state-law causes of action. In all pre-emption cases, and particularly in those in which Congress has legislated in a field which the States have traditionally occupied, we start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.

Medtronic, Inc. v. *Lohr*, 518 U.S. 470, 485 (1996) (internal quotations omitted); *see also Davis* v. *Davis (In re Davis)*, 170 F.3d 475, 481 (5th Cir. 1999) ("Deference to our federalism counsels a presumption that areas of law traditionally reserved to the states, like ... property law, are not to be disturbed absent the clear and manifest purpose of Congress." (internal quotations omitted)). The "presumption against displacing state law ... is just as strong in bankruptcy as in other areas of federal legislative power." *Pacific Gas & Elec. Co.* v. *California*, 350 F.3d 932, 943 (9th Cir. 2003), *cert. denied*, 543 U.S. 956 (2004); *Davis*, 170 F.3d at 481; *see also Sears, Roebuck & Co.* v. *O'Brien*, 178 F.3d 962, 966-967 (8th Cir. 1999) (federal bankruptcy law did not preempt Iowa law prohibiting debt collectors from contacting knowingly represented persons; although federal bankruptcy law is "expansive," Congress has not exclusively

regulated relationships between private lawyers and clients, an area typically within state's powers).

Where a federal statute does expressly preempt state law, a court "must in the first instance focus on the plain wording of the clause[.]" *Sprietsma* v. *Mercury Marine*, 537 U.S. 51, 62-63 (2002) (internal quotations omitted). In determining the scope of an express preemption provision, the court "move[s] on, as need be, to the structure and purpose of the Act in which [that provision] occurs." *New York State Conference of Blue Cross & Blue Shield Plans* v. *Travelers Ins. Co.*, 514 U.S. 645, 655 (1995). Where such an express preemption provision operates "in a field which the States have traditionally occupied," it receives a "narrow interpretation." *Medtronic*, 518 U.S. at 485 (internal quotations omitted).

The Bankruptcy Code, of course, contains no provision expressly preempting state law as to contractual obligations to pay attorneys' fees. And this Court has made clear that—while the ultimate touchstone is congressional intent—courts should be even more reluctant to assume that Congress intended to interfere with state laws that merely enforce contractual obligations, as opposed to affirmative state lawmaking or regulation. *See, e.g., Gibbons* v. *Ogden*, 22 U.S. (9 Wheat.) 1, 211 (1824) ("appropriate application of" Supremacy Clause is to "acts of the State Legislatures ... enacted in the exercise of [its] powers"); *Building & Constr. Trades Council* v. *Associated Contractors & Builders of Mass./R.I., Inc.*, 507 U.S. 218, 227 (1993) ("pre-emption doctrines apply only to state *regulation*"); *see also American Airlines, Inc.* v. *Wolens*, 513 U.S. 219, 228-229 (1995) (Airline Deregulation Act, which preempts state regulation of air carrier services, did not preempt state-law breach of contract claims filed by passengers against airline regarding frequent flier programs; contracts were "privately ordered obligations" and did not amount to a law, rule, regulation,

standard, or other provision having the force and effect of law under ADA preemption statute).[3]

Congress surely expressed no intention in the Bankruptcy Code to re-write contractual obligations to pay attorneys' fees. For example, there is certainly nothing in section 502 of the Bankruptcy Code, the provision governing the allowance of claims, suggesting that Congress intended to preempt state law on this issue. To the contrary, section 502 expressly reflects Congress's desire to defer to state law in determining the validity of a claim. A claim shall be allowed except to the extent that "such claim is unenforceable against the debtor ... under any agreement or applicable law[.]" 11 U.S.C. § 502(b)(1). Bankruptcy courts are thus obligated to examine applicable state law, not substitute an untethered federal common law, in determining the allowance of claims.

By contrast, there are several instances in the Bankruptcy Code in which Congress did reflect a clear desire to override the terms of state law and private contracts, and in each instance it made that intent clear. *See* 11 U.S.C. § 363(*l*) (governing use, sale, or lease of property) ("notwith-

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[3] *See also Duvall* v. *Bristol-Myers Squibb Co.*, 65 F.3d 392, 401 (4th Cir. 1995) (express warranty claim not preempted by Medical Device Amendment to Federal Food, Drug, and Cosmetic Act, which preempts state-imposed requirements on medical devices; to extent warranty claims based solely on voluntary promises made by warrantor, not duties imposed under state law, claims were not requirements imposed under state law), *vacated on other grounds*, 518 U.S. 1030 (1996); *American Auto. Mfrs. Ass'n* v. *Commissioner, Mass. Dep't Envtl. Prot.*, 998 F. Supp. 10, 21-24 (D. Mass. 1997) (Section 209(a) of the Clean Air Act, which preempted all state "standards" regarding vehicle emissions, did not apply to private Memoranda of Understanding between state agency and private automakers, as these were private, voluntary agreements, and were not "standards" within the section's preemptive scope; "courts generally restrict federal preemption to state laws, statutes, rules, regulations, and other state provisions having the force and effect of law" and have "made a clear distinction between state-imposed requirements and voluntary contractual agreements" (citations omitted)), *aff'd*, 208 F.3d 1, 7 (1st. Cir. 2000) ("[F]ederal preemption is generally confined to formal state laws and regulations and not applicable to contracts and other voluntary agreements.").

standing any provision in a contract, a lease, or applicable law"); *id.* § 365(e)(1) (governing executory contracts and unexpired leases) ("[n]otwithstanding a provision in an executory contract or unexpired lease, or in applicable law"); *id.* § 365(f)(1) ("[n]otwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law"); *id.* § 541(c)(1) (regarding property of the estate) ("notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law"); *id.* § 1124(2) (governing impairment of claims or interests) ("notwithstanding any contractual provision or applicable law"). And in the context of claims allowance, the various enumerated exceptions set forth in section 502(b) of the Bankruptcy Code expressly describe circumstances in which—notwithstanding the fact that a party may have a "right of payment," *id.* § 101(5)(A), under state law—that party's allowed "claim" under the Bankruptcy Code is calculated by a different means. *See, e.g., id.* § 502(b)(6) (providing for statutory caps on landlord claims for damages for the rejection of a real property lease).

In short, when Congress wished to preempt the terms of private agreements in the Bankruptcy Code, it has said so expressly. And it said nothing to suggest it intended to treat claims for attorneys' fees any differently from any other contractual obligation. On this and most other issues of the "allowance" of claims in bankruptcy, Congress expressly incorporated state substantive law into a bankruptcy court's analysis of the validity of a creditor's claim.

Nor can there be any suggestion that state law is "impliedly preempted" in this context. Such "conflict preemption" applies "where it is impossible for a private party to comply with both state and federal requirements, or where state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Sprietsma*, 537 U.S. at 64-65 (internal quotations omitted).

Here, there is neither an actual conflict between the Indemnity Agreements and section 502(b) nor do the Indemnity Agreements pose an obstacle to achieving Congress's full purposes and objectives in enacting section 502(b).

Rather, Travelers is seeking only the benefit of the bargain it negotiated with PG&E prior to PG&E's bankruptcy filing. There is no reason at all to believe that Congress intended the Bankruptcy Code to provide a basis for altering any and all state laws that are implicated by a bankruptcy filing—and even less reason to believe that it intended, beyond reducing a creditor's recovery to its *pro rata* distribution on account of its allowed claim, to provide a means for one party to re-write the parties' self-imposed contractual obligations.

To the contrary, the Bankruptcy Code generally takes state law as a given, and is construed to alter state law only in those circumstances in which it expressly so provides. And "[s]imply making a reorganization more difficult for a particular debtor . . . does not rise to the level of stand[ing] as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Baker & Drake, Inc.* v. *Public Serv. Comm'n (In re Baker & Drake, Inc.)*, 35 F.3d 1348, 1354 (9th Cir. 1994) (second alteration in original; internal quotations omitted). Permitting parties to a contract to file claims for attorneys' fees based on the property rights they possess under state law—just as they would if the very same arrangement were negotiated and implemented outside of bankruptcy—would by no means frustrate Congress's purpose in enacting section 502(b) or any other provision of the Code. To the contrary, it is fully consistent with the basic principle that a creditor's property rights in bankruptcy are identical to its rights outside bankruptcy.

Indeed, as far as federal policy is concerned, this Court has long accepted the proposition that even under the prevailing "American Rule," parties may provide by contract for a regime of fee-shifting. *See generally Fleischmann Distilling Corp.* v. *Maier Brewing Co.*, 386 U.S. 714, 717 (1967) (attorneys' fees are not recoverable "in the absence of a statute or enforceable contract providing therefor"); *Summit Valley Indus., Inc.* v. *Local 112, United Bhd. of Carpenters and Joiners of Am.*, 456 U.S. 717, 721 (1982) ("[u]nder the American Rule it is well established that attorney's fees are not ordinarily recoverable in the absence of a statute or enforceable contract providing therefore" (internal quota-

tions omitted)); *Hall* v. *Cole*, 412 U.S. 1, 4 (1973) ("the traditional American Rule ordinarily disfavors the allowance of attorneys' fees in the absence of statutory or contractual authorization" (footnote omitted)); *Alyeska Pipeline Serv. Co.* v. *Wilderness Soc'y*, 421 U.S. 240, 257 (1975) ("the general rule [is] that, absent statute or enforceable contract, litigants pay their own attorneys' fees").

C. The Proper Analysis Is Simply Whether The Disputed Attorneys' Fees Are Permissible Under The Indemnity Agreements

The court of appeals below relied on its decision in *In re Fobian*, 951 F.2d 1149, to conclude that "attorney fees are not recoverable in bankruptcy for litigating issues 'peculiar to federal bankruptcy law.'" Pet. App. 3a (quoting *Fobian*, 951 F.2d at 1153). The Ninth Circuit characterized Travelers' claim as an attempt "to recover fees in bankruptcy for objections to proposed reorganization plans and related bankruptcy proceedings," and thus "[t]he resolution of all of these proceedings was governed entirely by federal bankruptcy law." *Id.* 2a-3a. That is simply incorrect. The fact that federal bankruptcy law applied to the underlying proceedings provides no basis at all for creating a federal common law—independent of whether state law would enforce a contractual obligation—regarding the validity of Travelers' claim for attorneys' fees.

It is thus unsurprising that other courts, those that adhere to the congressional design reflected in the Bankruptcy Code, have rejected the Ninth Circuit's analysis, instead permitting attorneys' fees to be part of an allowed claim where otherwise applicable state law would so provide. *See Alport* v. *Ritter (In re Alport)*, 144 F.3d 1163, 1168 (8th Cir. 1998); *Davidson* v. *Davidson (In re Davidson)*, 947 F.2d 1294, 1298 (5th Cir. 1991); *TranSouth Fin. Corp.* v. *Johnson*, 931 F.2d 1505, 1509 (11th Cir. 1991); *Martin* v. *Bank of Germantown (In re Martin)*, 761 F.2d 1163, 1168 (6th Cir. 1985); *see also* 4 *Collier on Bankruptcy* ¶ 506.04 (15th ed.) (*Fobian* analysis "inverts the proper analysis" because "a claim that is valid under state law is allowable in bankruptcy unless

some provision of the Bankruptcy Code expressly *disallows* it").

The Fourth Circuit has specifically and correctly criticized Ninth Circuit's analysis on the ground that it substitutes federal law for applicable state law, noting that *Fobian* "inappropriately focuses on the presence of issues peculiar to bankruptcy law, rather than on whether the attorneys' fees are properly taken in furtherance of the [contract] and applicable state law." *Three Sisters Partners LLC* v. *Harden (In re Shangra-La, Inc.)*, 167 F.3d 843, 848 (4th Cir. 1999). Section 502(b)(1) instructs the bankruptcy court to determine whether the claim for attorneys' fees are enforceable under "any agreement or applicable law." 11 U.S.C. § 502(b)(1). Consequently, the contracts between Travelers and PG&E—the Indemnity Agreements—must serve as "the measure of their rights," *Chicago, Milwaukee*, 791 F.2d at 529, and not federal common law.

Because the bankruptcy court below incorrectly denied Travelers' claim as a matter of federal bankruptcy law, it never examined the legitimacy of the claim with respect to the terms of the Indemnity Agreement and applicable state contract law. Accordingly, this Court should reverse the Ninth Circuit's ruling affirming the bankruptcy court's decision and remand for such a determination.

II. THE CREATION OF A "FEDERAL COMMON LAW" OF CLAIMS ALLOWANCE WOULD INVITE FORUM SHOPPING INTO BANKRUPTCY

As this Court observed in *Butner*, the "[u]niform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving 'a windfall merely by reason of the happenstance of bankruptcy.'" *Butner*, 440 U.S. at 55 (quoting *Lewis* v. *Manufacturers Nat'l Bank*, 364 U.S. 603, 609 (1961)).

These goals are critically important, as both common sense and actual experience demonstrate the very palpable risk that whenever the question of claims allowance is governed in bankruptcy by different standards than those that

prevail outside of bankruptcy, there is a risk that litigants will seek to forum shop into bankruptcy in order to obtain a litigation advantage, without regard to the underlying purposes of bankruptcy law. In response, the courts have been required to develop the doctrine of "good faith," designed to limit access to the chapter 11 bankruptcy process to those debtors whose bankruptcy cases serve legitimate reorganizational purposes, and not those who are led into bankruptcy by a desire to forum shop.

This risk is already present in those few areas where the Bankruptcy Code expressly provides that the allowance of claims is to be determined in a manner that differs from state law. For example, section 502(b)(6) of the Bankruptcy Code provides that a landlord's claim for damages for rejection of a long-term lease of real property is subject to a statutory cap. In *NMSBPCSLDHB, L.P.* v. *Integrated Telecom Express, Inc. (In re Integrated Telecom Express, Inc.)*, 384 F.3d 108 (3d Cir. 2004), the Third Circuit was thus required to address the circumstance of a party that filed for bankruptcy in the absence of any financial distress or legitimate need for bankruptcy protection, but merely in order to take advantage of this particular provision of the Code.

In response, the Third Circuit held that such a bankruptcy case is not filed in good faith, and thus is subject to dismissal "for cause" under section 1112(b) of the Bankruptcy Code. 384 F.3d at 129-130. The court held that Integrated Telecom's petition aimed neither to preserve a going concern nor to maximize property available to satisfy creditors—the two objectives that chapter 11 of the Bankruptcy Code seeks to foster. Instead, the Third Circuit observed Integrated Telecom's likely motive was simply "to gain a litigation advantage" against its landlord by invoking the Code's cap on landlord damages. *Id.* at 124-125.

This risk of forum shopping is particularly acute in the context of mass-tort bankruptcies, in which companies with alleged liability for the sale or manufacture of, for example, asbestos-containing products seek protection in bankruptcy. In certain of these cases, companies whose non-insurance assets may be insubstantial or have already been largely de-

pleted are led into bankruptcy by the tort claimants, who hope to create, in bankruptcy, a more lax claims allowance process that will drive up the company's "liability," and thus create for them a strategic litigation advantage over the company's insurers. *See generally Century Indem. Co.* v. *Congoleum Corp. (In re Congoleum Corp.)*, 426 F.3d 675 (3d Cir. 2005); Mark D. Plevin et al., *Pre-Packaged Asbestos Bankruptcies: A Flawed Solution*, 44 S. Tex. L. Rev. 883 (2003).

Affirming the decision below would open the door to precisely this type of gamesmanship. As this Court observed in *Butner*, no litigant should stand to reap a windfall "merely by reason of the happenstance of bankruptcy." 440 U.S. at 55 (internal quotations omitted).

* * * * *

To facilitate the economic rehabilitation of individuals or troubled businesses, bankruptcy law provides powerful tools with which a court can alter settled legal expectations. Debts can be discharged. Leases can be cut short. All this is possible because federal bankruptcy power, when exercised under federal law, trumps the state law foundations on which the debtor and its creditors ordered their respective rights. *Sturges* v. *Crowninshield*, 17 U.S. 122, 193-194 (1819). The strong medicine bankruptcy law provides thus comes with a crucial limitation: it can only be exercised when it would serve a bankruptcy goal that Congress has identified. That is, "[b]ankruptcy law changes nonbankruptcy law only when the purposes of bankruptcy law require it," Douglas G. Baird, *The Elements of Bankruptcy* 5 (4th ed. 2006), and bankruptcy law suspends state law only where such preemption is express or implied, i.e., "to the extent of the actual conflict with the system provided by the Bankruptcy Act." *Butner*, 440 U.S. at 54 n.9.

The Ninth Circuit's decision below breaks with this critical and long-standing principle, and fundamentally upsets the relationship between bankruptcy and nonbankruptcy law.

CONCLUSION

For the foregoing reasons, the judgment below should be reversed.

Respectfully submitted,

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